MORRISON | FOERSTER

2000 PENNSYLVANIA AVE., NW
WASHINGTON, D.C.
20006-1888

TELEPHONE: 202.887.1500
FACSIMILE: 202.887.0763

WWW.MOFO.COM

MORRISON & FOERSTER LLP
NEW YORK, SAN FRANCISCO,
LOS ANGELES, PALO ALTO,
SAN DIEGO, WASHINGTON, D.C.
NORTHERN VIRGINIA, DENVER,
SACRAMENTO, WALNUT CREEK
TOKYO, LONDON, BRUSSELS,
BEIJING, SHANGHAI, HONG KONG

January 31, 2011

Writer's Direct Contact
(202) 887-1519
DMeyer@mofo.com

228733

VIA ELECTRONIC FILING

Cynthia T. Brown
Chief, Section of Administration
Office of Procedures
Surface Transportation Board
395 E Street, S.W.
Washington, D.C. 20423-0001

Re: STB Ex Parte No. 704

Dear Ms. Brown:

Attached for electronic filing in the above-referenced docket are the Comments of Norfolk Southern Railway Company in response to the Board's Corrected Notice served October 25, 2010 in this docket.

Also attached is a written summary of testimony to be offered by David Lawson, Norfolk Southern's Vice President, Industrial Products, at the hearing scheduled for February 24, 2011 in this docket. Norfolk Southern requests that Mr. Lawson be given ten minutes to present his testimony at the February 24 hearing.

Thank you for your assistance.

Sincerely,

David L. Meyer

Attachments

cc (with attachments): John M. Scheib, Esq.

BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO. 704

REVIEW OF COMMODITY, BOXCAR, AND TOFC/COFC EXEMPTIONS

COMMENTS OF NORFOLK SOUTHERN RAILWAY COMPANY

James A. Hixon
John M. Scheib
Greg E. Summy
Christine I. Friedman
Norfolk Southern Railway Company
Three Commercial Place
Norfolk, VA 23510

David L. Meyer
Nicholas A. Datlowe
Morrison & Foerster LLP
2000 Pennsylvania Avenue, N.W.
Suite 6000
Washington, D.C. 20006

Attorneys for Norfolk Southern Railway Company

Dated: January 31, 2011

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EX PARTE NO. 704

REVIEW OF COMMODITY, BOXCAR, AND TOFC/COFC EXEMPTIONS

COMMENTS OF
NORFOLK SOUTHERN RAILWAY COMPANY

Norfolk Southern Railway Company ("NS") submits these Comments in response to the Board's Corrected Notice served October 25, 2010 ("Corrected Notice"), and its decision served November 19, 2010.

INTRODUCTION

The Board's Notice states that the Board's decision to hold a hearing was prompted by "informal inquiries questioning the relevance and/or necessity" of certain of the exemptions established by the Board and its predecessor pursuant to 49 U.S.C. § 10502.[1] The Board seeks comments on three issues concerning the Commodity, Boxcar and TOFC/COFC exemptions (which for convenience we refer to herein as the "exemptions" or the "commodity exemptions"): "the effectiveness of the exemptions in the marketplace; whether the rationale behind any of the exemptions should be revisited; and whether the exemptions should be subject to periodic review."[2]

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1 Corrected Notice, at 3.

2 *Id.*

As we explain in these Comments, NS believes there is no good reason for this hearing. The exemptions continue to fulfill Congress's broad and enduring mandate that rail service be exempted from regulation except to the limited extent necessary to protect shippers from the abuse of market power. As the Department of Transportation explained before the Board in 2006, "Congress directed that the exemption authority contained in the Staggers Rail Act be used whenever continued regulation is not necessary. That command remains intact today."[3] Against this statutory backdrop, further proceedings to revisit the existing exemptions are unwarranted.

Moreover, there is no reason for the Board to be concerned that the exemptions inhibit shippers from seeking regulatory protection when needed. To the extent that particular shippers (or groups of shippers) of exempt commodities believe that the railroad serving them is abusing its market power, there is no obstacle to their invoking the Board's revocation power to secure available regulatory protections. Experience shows that the Board has partially revoked the exemptions when justified.

That experience also confirms, however, that railroads continue to face competition for exempted transportation services that is no less pervasive than when the Board and its predecessor granted the exemptions. Indeed, competition is more robust than ever, partly as a result of the investments and efficiencies made possible by Congress's and the Board's deregulatory efforts. At bottom, there simply is no problem in need of a solution.

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[3] Comments of the United States Department of Transportation, Ex Parte No. 661, *Rail Fuel Surcharges*, (Oct. 2, 2006), at 4-5 (citations omitted).

It is curious that the Board would consider revoking exemptions and reinstituting regulation – in direct conflict with the governing statutes and Congressional intent – at the same time as the President of the United States is asking regulatory agencies to pursue the opposite course. On January 18, 2010, President Barack Obama issued an Executive Order requiring regulatory agencies to adhere to several "basic tenets," including the obligation "to consider . . . how best to *reduce burdens for American businesses* and consumers," "to seek . . . the *least burdensome approaches*," and "to review old regulations so that *rules which are no longer needed can be modified and withdrawn.*"[4] President Obama explains that his goal was to "remove outdated regulations that stifle job creation and make our economy less competitive."[5] The President's clear message is for agencies to remove regulatory burdens wherever possible, and not to expand regulation unnecessarily.

NS submits that the Board's Notice (which indirectly questions "the relevance and/or necessity" of existing exemptions) approaches the issue of commodity exemptions from the wrong end of the telescope. To carry out its statutory responsibilities, the Board should be actively pursuing the exemption of additional commodities for which regulation is no longer necessary to protect shippers from the abuse of market power. NS has identified four such commodities that, notwithstanding the good efforts of the Board

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[4] "Regulatory Strategy," White House Blog (Jan. 18, 2011), *available at* http://www.whitehouse.gov/blog/2011/01/18/regulatory-strategy (last visited Jan. 25, 2011) (emphasis added).

[5] Barack Obama, "Toward a 21st-Century Regulatory System," *The Wall Street Journal*, Jan. 18, 2011 at A17 (Obama Op. Ed). In the Order itself, the President commanded that "each agency shall identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public." Executive Order No. 13,563, Jan. 18, 2011.

and the ICC before it in granting a series of commodity exemptions, unnecessarily remain subject to the full array of Board-administered regulation. NS requests that the Board commence proceedings pursuant to Section 10502(a) to review the appropriateness of exempting these additional commodities from regulation.

I. THE STATUTORY FRAMEWORK EXPRESSED CONGRESS'S DEREGULATORY MANDATE

The ICC and Board adopted the exemptions in response to Congress's mandate that the agency free the railroads of unnecessary regulatory burdens. Congress began in 1976 by providing the ICC permissive exemption authority in the Railroad Revitalization and Regulatory Reform Act ("4-R Act"). With the Staggers Rail Act of 1980 ("Staggers Act"), Congress replaced that permissive authority with an outright command that the agency use its exemption power to eliminate unnecessary regulation. Sixteen years later, Congress amplified this mandate with new statutory language in the Interstate Commerce Commission Termination Act ("ICCTA") requiring the Board to exempt rail service from regulation to the "maximum extent" possible consistent with applicable law.[6] This steady progression resulted in the statutory framework that remains in place today and precludes the Board from materially altering its longstanding deregulatory approach.

A. The Statutory Framework Encourages Extensive Deregulation of Rail Transportation

The statutory scheme in place since the Staggers Act heavily favors deregulation. As set forth in 49 U.S.C. § 10502(a), Congress has directed the Board to liberally grant exemptions from regulation. Specifically:

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[6] *See* 49 U.S.C. § 10502(a).

> [T]he Board ***to the maximum extent consistent with this part, shall*** exempt a person, class of persons, or a transaction or service whenever the Board finds that the application in whole or in part of a provision of this part - (1) is not necessary to carry out the transportation policy of section 10101 of this title; and (2) either - (A) the transaction or service is of limited scope; or (B) the application in whole or in part of the provision is not needed to protect shippers from the abuse of market power.

(emphasis added).

The Board has consistently recognized that the statutory mandate to exempt traffic from regulation is "framed in very broad terms."[7] The exemptions were required to achieve Congress's goal "to remove regulatory burdens and to allow the marketplace to influence decisions in the rail industry."[8] Accordingly, the statute imposes on the Board an "*affirmative duty* . . . to 'pursue partial and complete exemptions from remaining regulation,'"[9] and "*favors exemptions* from regulation whenever appropriate."[10] Stated succinctly, "[u]nder 49 U.S.C. 10502(a), the Board (like the ICC before it) has been directed to exempt entire categories of traffic from the regulatory provisions of the Interstate Commerce Act, to the maximum extent consistent with the Act."[11]

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[7] *Exemption from Regulation – Boxcar Traffic*, 367 I.C.C. 424, 428 (1983) ("*Boxcar Exemption Decision*"), *aff'd sub nom. Brae Corp. v. United States*, 740 F.2d 1023 (D.C. Cir. 1984) ("*Brae v. U.S.*"), *cert. denied*, 471 U.S. 1069 (1985).

[8] *Brae v. U.S.*, 740 F.2d at 1055.

[9] *Boxcar Exemption Decision*, 367 I.C.C. at 428 (emphasis added; quoting H.R. Rep. No. 96-1430, at 105 (1980)).

[10] *WTL Rail Corporation Petition for Declaratory Order & Interim Relief*, STB Docket No. 42092 (served Feb. 17, 2006), at 3 (emphasis added).

[11] *Rail Fuel Surcharges*, STB Ex Parte No. 661 (served Jan. 26, 2007), at 12. *See also, e.g., Improvement of TOFC/COFC Regulation*, 364 I.C.C. 731, 732 (1981) ("TOFC/COFC Exemption Decision") ("We believe that our proposed exemption is consistent with the congressional intent

(footnote continued on next page ...)

This mandate implements critical elements of the Rail Transportation Policy. It "allow[s], to the maximum extent possible, competition and demand for services to establish reasonable rates for rail transportation," 49 U.S.C. § 10101(1); it "minimize[s] the need for Federal regulatory control over the rail transportation system," *id.* § 10101(2); it helps "ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes," *id.* § 10101(4); and it "foster[s] sound economic conditions in transportation to ensure effective competition and coordination between rail carriers and other modes," *id.* § 10101(5).

B. Congress's Ratification and Amplification of the Exemption Mandate in Enacting ICCTA Precludes the Board from Changing Course Towards Reregulation

The evolution of the current statutory language and exemption regime confirms that the Board has been given a broad mandate to exempt – regardless of the economic health of the railroads or the effects or benefits of the exemption – and afforded much narrower authority to revoke such exemptions.

When Congress enacted ICCTA in 1996, it had before it 16 years of deregulatory experience under the Staggers Act – including the many commodity exemptions the ICC had granted in response to Congress's deregulatory mandate. Drawing on that experience, Congress chose to expand the fundamental deregulatory command of Section 10505 of the Staggers Act. A close examination of what ICCTA did and did not change leaves no doubt that the statutory mandate favoring deregulation is stronger than ever.

(... footnote continued from previous page)

that we *vigorously pursue exemptions* from economic regulation in the railroad area where regulatory control appears unnecessary to protect against abuses of market power" (emphasis added).).

During the 16 years between the Staggers Act and ICCTA, railroads had taken advantage of their new commercial freedoms: they had become much more efficient, they had invested heavily in improved service offerings, and many of them had made some progress towards revenue adequacy. The improvement in the railroads' financial condition was a crucial measure – and indeed sine qua non – of the success of the deregulatory scheme, which was designed to benefit railroads and their customers. As the Department of Transportation aptly summarized in its testimony before Congress in 1995:

> As a result of the Staggers Act reforms, the health of the industry has improved significantly: for the 12 months ending September 30, 1994, the railroad industry earned an average 8.4 percent return on its net investment base, doubling its return of 1980 while maintaining its market share of about 38 percent. Carriers have invested approximately $190 billion in infrastructure and equipment since 1980, allowing much needed rehabilitation and modernization of the nationwide rail system.
>
> Best of all, the rail industry's transformation has not been at the expense of shippers. Overall real (inflation-adjusted) freight rates have dropped 1.6 percent per year since 1980 – over 33 percent overall. Coal rates have declined 1.8 percent per year; grain and chemicals 1.2 percent; rates for miscellaneous mixed shipments – a key component of intermodal traffic – have dropped 2.2 percent annually. Clearly, a wide cross-section of rail shippers – including some thought to be captive – have benefited from Staggers Act reforms.
>
> The rail industry is now relatively healthy, *and the critical freedoms of the Staggers Act must be maintained if it is to remain financially successful. . . .*"[12]

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[12] Testimony of Joseph Canny, Deputy Assistant Secretary for Transportation Policy, U.S. Department of Transportation, before the Subcommittee on Railroads of the House Transportation and Infrastructure Committee (Feb. 22, 1995) ("DOT ICCTA Testimony"), at 212 (emphasis added).

(footnote continued on next page ...)

The positive feedback that Congress received regarding the success of the Staggers Act reforms and the ICC's aggressive pursuit of additional deregulation via its exemption authority left no doubt that Congress should press forward with further deregulation when it shifted regulatory responsibility to the Board. Based on the record of deregulatory success, both DOT and the ICC opined that deregulation was working and recommended that the responsible regulatory agency – now the Board – continue to have the administrative authority to remove unnecessary regulatory burdens and continue to make aggressive use of that authority.[13] Congress shared this view, concluding that the Board's mandate to grant exemptions remained a "*crucially important* delegated power to expand existing statutory deregulation through administrative action."[14]

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DOT reaffirmed this view even more strongly ten years later, during the Board's 2005 review of experience with deregulation on the 25th anniversary of the Staggers Act:

> The Department of Transportation considers the Act a resounding success. We do so because in sum the statute did what it was designed to do. It revitalized the railroad industry and by so doing benefitted shippers and consumers throughout the economy. Twenty-five years ago this was an industry, as you have said, marked by decline in all major respects: high rates, low returns on investment, eroding demand, low modal traffic share and excess capacity.

The 25th Anniversary of the Staggers Rail Act of 1980: A Review and Look Ahead, STB Ex Parte No. 658, Transcript of Hearing (Oct. 19, 2005), pp. 14-15.

[13] DOT recommended to Congress that the "authority to lift regulatory requirements administratively should be retained, and used aggressively" because "[t]he exemption provision has proven to be one of the Staggers Act's most significant innovations." DOT ICCTA Testimony, at 217. Likewise, the ICC's 1994 "Study of Interstate Commerce Commission Regulatory Responsibilities" recommended that the ICC "continue to push its exemption authority aggressively." 1994 ICC Study (Oct. 25, 1994), at 7.

[14] Report of the House Committee on Transportation and Infrastructure, H.R. Rep. 104-311, at 96 (1995), *reprinted in* 1995 U.S. Code Cong. & Admin. News 793, 808 ("ICCTA House Report") (emphasis added).

Reflecting this conclusion, new Section 10502 preserved the basic framework of the Staggers Act's exemption mandate (previously codified at 49 U.S.C. § 10505), leaving intact both the requirement that the Board "*shall*" grant exemptions, as well as the Board's authority to revoke an exemption only to the extent that some regulation proved "necessary." This structure alone confirms that Congress did not regard changes over the preceding 16 years as calling into question the desirability of continued deregulation.[15]

But Congress went further, making three substantive changes to the statute that amplified its policy that the Board grant exemptions liberally and revoke them only upon a showing of necessity.

First, ICCTA *heightened* the Board's obligation to exempt rail service from regulation by commanding that the Board not only "*shall*" grant exemptions, but that it shall do so "***to the maximum extent consistent with this part.***"[16] Congress wanted to leave no doubt that exemptions were desirable and so made "it an explicit part of the agency's statutory duty to utilize exemptions to the maximum extent permissible under the law."[17]

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[15] *See, e.g., United States v. G. Falk & Brother*, 204 U.S. 143 (1907) (reenactment of statute in face of longstanding agency policy constitutes adoption of that policy).

[16] 49 U.S.C. § 10502(a) (emphasis added).

[17] ICCTA House Report, at 96. *See also* Joint Explanatory Statement of the Committee of Conference, H.R. Rep. No. 104-422, at 169 (1995), *reprinted in* 1995 U.S. Code Cong. & Admin. News 850, 853 ("ICCTA Conference Report").

Second, Congress removed "restrictions on use of the exemption power in matters relating to intermodal ownership."[18] This change stemmed from Congress's judgment that "other modes of transportation are sufficiently competitive (as is the rail industry) as to make the former categorical immunization of intermodal ownership from administrative exemption obsolete and unnecessary."[19]

Third, Congress *diminished* the Board's authority to revoke those exemptions by revising the procedural mechanism for initiating a revocation proceeding. The previous provision had not specified how a revocation proceeding could be commenced, and thus suggested that one could be commenced "on [the agency's] own initiative."[20] ICCTA added language specifying that a revocation proceeding could be commenced only upon "a request for revocation."[21] In explaining the new revocation provision, Congress made clear that it did not want the Board to relax the strict standards for revoking exemptions. To the contrary:

> When considering a revocation request, the Board should continue to require demonstrated abuse of market power that can be remedied only by reimposition of regulation or that regulation is needed to carry out the national transportation policy. The Conference expects the Board to examine all competitive transportation factors that restrain rail carriers' actions and that affect the market for transportation of the particular commodity or type of service for which revocation has been requested.[22]

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18 ICCTA House Report, at 96.

19 *Id.*

20 *See* former 49 U.S.C. § 10505(b), (d).

21 49 U.S.C. § 10502(d).

22 ICCTA Conference Report, at 169.

The statutory framework that Congress amplified and strengthened in 1996 remains in place today[23] and constrains any action the Board might consider taking with regard to existing exemptions.

C. The Dichotomy Between the Expansive Power to Exempt and the Limited Power to Revoke an Exemption Reinforces the Deregulatory Preference in the Statutory Regime

In contrast to the express language of the statute mandating exemptions to the "maximum extent," the statute narrowly bounds the Board's discretion to reconsider or revoke exemptions it has previously granted. The narrow scope of the Board's revocation authority flows directly from Congress's desire that rail transportation be deregulated to the maximum extent possible.

The Board's discretion is limited both substantively and procedurally to prevent an undermining of the broad preference for exemptions.

- *First*, the Board may re-regulate exempt conduct only upon a determination that "application in whole or in part of a provision of this part to the person, class, or transportation is *necessary* to carry out the transportation policy of section 10101 of this title."[24]
- *Second*, Congress did not empower the Board to conduct any periodic review or general reconsideration of previously-granted rail exemptions, despite mandating such reviews with respect to other aspects of the Board's regulatory portfolio.[25]

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[23] Indeed, legislation was introduced in the 111th Congress that would have revised the statutory scheme regarding exemptions. *See* S. 2889, 111th Cong. (2010). The failure of that legislation constitutes endorsement of the manner in which the Board has implemented the existing regime. *See Bob Jones Univ. v. United States*, 461 U.S. 574 (1983) (Congress endorses regulatory policy when it knows of statutory interpretation and declines to change statute).

[24] 49 U.S.C. § 10502(d) (emphasis added).

[25] *See, e.g.*, 49 U.S.C. § 13703(c)(2) (mandating Board proceedings to conduct periodic reviews of approved motor carrier rate agreements).

- *Third*, the statute provides that whereas the Board may begin a proceeding to exempt transportation "on its own initiative," it may consider revoking exemptions only upon "receipt of a request for revocation."[26]

Thus, Congress plainly intended that exemptions be the rule, and regulation (or reregulation) the exception. It follows that the agency's role in revoking exemptions is confined to a review of specific facts and circumstances through a case-by-case review, upon receipt of a formal request, to determine whether application of some aspect of the regulatory regime is *necessary*, notwithstanding the generally-applicable market conditions that justified the exemption.[27]

As the court of appeals explained, this basic dichotomy between the expansive mandate to exempt and narrowly-confined discretion to revoke was "an 'important cornerstone'" of the Staggers Act:

> Further, as to the Commission's exercise of its exemption authority, the Conference Report states that "the conferees expect that as many as possible of the Commission's restrictions on changes in prices and services by rail carriers will be removed and that the Commission will adopt a policy of reviewing carrier actions after the fact to correct abuses of market power." H.R. Rep. No. 96-1430, 96th Cong., 2d Sess. 105 (1980), *reprinted in* 1980 U.S. Code Cong. & Ad. News 4110, 4137.[28]

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[26] 49 U.S.C. § 10502 (b), § 10502(d). *See also* 49 U.S.C. § 11701(a) (Board may act only upon complaint unless otherwise specified).

[27] As stressed by the ICC, a party seeking revocation must overcome the agency's original finding of competition: "We also wish to emphasize that a revocation petition focuses on traffic that has previously been exempted from Commission regulation on the basis of this agency's conclusion that the marketplace itself is sufficiently competitive so as not to require continued government regulation. Thus, a party [seeking revocation] has a burden of showing that our prior findings supporting the initial exemption were clearly wrong, or that changed circumstances require us to revisit them." *Rail General Exemption Authority – Miscellaneous Agricultural Commodities – Petition of G&T Terminal Packaging Co., Inc., to Revoke Conrail Exemption*, 8 I.C.C.2d 674, 677 (1992) (declining petition for revocation), *aff'd sub nom. Mr. Sprout, Inc. v. United States*, 8 F.3d 118 (2d Cir. 1993).

[28] *American Trucking Assoc. v. ICC*, 656 F.2d 1115, 1119-20 (9th Cir. 1981).

The Board has similarly noted this dichotomy when it has explained that it will "liberally exempt[] carriers from regulatory requirements and review[] carrier actions after the fact to correct abuses of market power."[29]

D. The Bar for Proving That Revocation is Warranted Is High and Requires a Particularized Showing that Regulation is Necessary to Remedy the Abuse of Market Power

Because the goal of the statute is to deregulate to the maximum extent, Congress has repeatedly made clear that the bar to revoke an exemption is a high one:

> When considering a revocation request, the Board should continue to require ***demonstrated abuse of market power that can be remedied only by re-imposition of regulation*** or that regulation is needed to carry out the national transportation policy. The Conference ***expects the Board to examine all competitive transportation factors*** *that restrain rail carriers' actions and that affect the market for transportation of the particular commodity or type of service* for which revocation has been requested.[30]

Accordingly, the Board and the courts have consistently held that revocation is appropriate only in those specific instances where a shipper is able to demonstrate that application of a particular regulatory requirement is necessary to protect the shipper from an abuse of market power.[31] The Board has ruled that, "[i]n considering whether to

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[29] *Pejepscot Industrial Park, Inc., d/b/a Grimmel Industries–Petition for Declaratory Order*, STB Finance Docket No. 33989 (served May 15, 2003), at 6 n.12.

[30] ICCTA Conference Report, at 168 (emphasis added). In enacting the Staggers Act, Congress similarly observed that it "expect[ed] that the Commission will adopt a policy of reviewing carrier actions after the fact to correct abuses of market power." H.R. Rep. No. 96-1430, at 105 (1980), *reprinted in* 1980 U.S. Code Cong. & Admin. News 4110, 4137.

[31] The focus on market power makes sense in the context of the rail transportation policies implicated by the commodity exemptions. Although the statute conditions issuance of an exemption on a finding that regulation is "not necessary to carry out the transportation policy of section 10101," all of the pertinent elements of the rail transportation policy point in the direction of deregulating except to the extent necessary to correct abuses that might arise in the absence of effective competition. Deregulation is the affirmative aim of Sections 10101(2) and (7). Sections 10101(1), (4), (5) and (6) seek to have market forces (competition and the demand for services),

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revoke an exemption, 'the first thing we look at . . . is whether the carrier possesses substantial market power. If it does not, then there is generally no basis for revoking an exemption.'"[32] Only if market power is present does the Board then proceed to "'focus on whether regulation is necessary to protect against carrier abuse of shippers as a result of such market power.'"[33]

In the three decades since the Staggers Act, the Board and its predecessor have consistently adhered to this approach, allowing shippers to invoke regulatory protections by seeking revocation, but demanding a particularized showing regarding their *need* for protection from a carrier's abuse of market power. Shippers have shown no reluctance to bring before the Board complaints about railroad rates and practices involving exempt transportation, and the Board has shown itself open to considering those complaints so long as the shipper can clear the hurdle of presenting particularized evidence demonstrating the need for reregulation to address the potential abuse of market power.

The Board has treated each case on its own merits. On the one hand, the Board revoked the applicable commodity exemption (for crushed or broken stone, sand, and gravel) in response to a complaint that one carrier was blocking another's ability to fulfill its common carrier service obligation.[34] The Board did so only after making

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rather than regulation, establish reasonable rates for transportation by rail. And Section 10101(3) seeks to ensure that carriers are able to earn adequate revenues.

[32] *Rail Fuel Surcharges*, STB Ex Parte No. 661 (served Jan. 26, 2007), at 12 (quoting *Rail Exemption Misc. Agricultural Commodities*, 8 I.C.C.2d 674, 682 (1992)).

[33] *Id.*

[34] *Granite State Concrete Co., Inc. & Milford-Bennington R.R. v. Boston & Maine Corp. & Springfield Terminal Ry.*, STB Docket No. 42083 (served Sept. 15, 2003).

particularized findings that the shipper "lacks the competitive service options that were the basis for the original class exemption."[35] On the other hand, in cases where shippers (or others) have sought revocation of a commodity exemption, the Board (or the ICC) has declined to revoke the applicable exemption when there had not been the requisite particularized showing that regulation was necessary to protect against the abuse of market power. In *WTL Rail Corporation Petition for Declaratory Order & Interim Relief*,[36] for example, the Board declined to revoke the TOFC/COFC exemption because shippers would continue to "have an array of competitive options for obtaining TOFC service and equipment," which in turn would "effectively constrain the railroads' market power with respect to TOFC service and equipment."[37]

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35 *Id.* at 7. As the Board explained in a subsequent decision, the "record of [the carrier's] conduct show[ed] that Granite State [merited] immediate access to the Board's processes to protect the shipper from the risk of market power abuse." *Granite State Concrete Co., Inc. & Milford-Bennington R.R. v. Boston & Maine Corp. & Springfield Terminal Ry.*, STB Docket No. 42083 (served Sept. 24, 2004), at 5.

36 STB Docket No. 42092 (served Feb. 17, 2006).

37 *See also, e.g., American Rail Heritage, Ltd., d/b/a Crab Orchard & Egyptian R.R, Transportation Concepts, Inc., & The Grafton & Upton R.R. v. CSX Transportation, Inc.*, ICC Docket No. 40774 (served June 16, 1995) (declining to revoke the TOFC/COFC exemption to require the mandatory interchange of intermodal trailers because the complainant failed to show that over-the-road movement of trailers provided inadequate competition); *Rail General Exemption Authority – Miscellaneous Agricultural Commodities – Petition of G&T Terminal Packaging Co., Inc., to Revoke Conrail Exemption*, 8 I.C.C.2d 674, 682 (1992) ("Although Conrail has imposed surcharges on petitioners' traffic, in our view it does not possess enough market power to warrant regulation."), *aff'd sub nom., Mr. Sprout, Inc. v. United States*, 8 F.3d 118 (2d Cir. 1993); *FMC Wyoming Corp. & FMC Corp. v. Union Pacific R.R.*, 4 S.T.B. 699, 711 n.18 (2000) (declining to revoke exemption in stand-alone-cost rate case because railroad lacked market dominance over the movements at issue and therefore Board "could not review the reasonableness of the rates that applied to these coke movements even if [it] were to revoke the exemption").

The Board has also declined to revoke the commodity exemptions based on its conclusion that the carrier had not abused whatever market power it might have possessed. For example, in *Bolen–Brunson–Bell Lumber Company, Inc. v. CSX Transportation, Inc.*, STB Finance Docket No. 34236 (served May 15, 2003), the Board declined to revoke the lumber and

(footnote continued on next page ...)

II. THE COMMODITY, BOXCAR, AND TOFC/COFC EXEMPTIONS HAVE BEEN EFFECTIVE AT FURTHERING CONGRESS'S STATUTORY MANDATE AND RAIL TRANSPORTATION POLICY OBJECTIVES

The Board's Notice asks whether the exemptions have been "effective." Although effectiveness is not the standard for revocation, the answer is nonetheless resoundingly in the affirmative. In fact, the exemptions continue to play an important role in the transportation marketplace.

A. Although the Statute Does Not Demand That Exemptions Bring Affirmative "Benefits," They Have Been and Remain Beneficial

The potential for affirmative benefits has never been the touchstone for evaluating the appropriateness of exempting particular traffic, since exemption is mandatory unless regulation is essential. The ICC has long recognized this basic principle. In granting its *Boxcar Exemption,* for example, the ICC emphasized that it had "focused on claims of negative effects of [an] exemption, since [the statute] requires [it] to find continued regulation necessary" in order to reject an exemption.[38] Nonetheless, the exemptions under review in this proceeding have generated considerable affirmative benefits and continue to be important in today's marketplace.

First and foremost, the exemptions have advanced the Rail Transportation Policy by (1) allowing market forces rather than regulation to govern the railroads' provision of exempted services; (2) minimizing the need for regulation; and (3) ensuring effective

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wood products exemption after concluding that, regardless of whether the carrier possessed market power, it had not abused that power "or otherwise acted inappropriately, in initiating and maintaining [an] embargo." *Id.* at 2.

[38] 364 I.C.C. at 445-46.

competition between railroads and other modes.[39] The benefits of the Staggers Act deregulatory reforms have been extensively treated in other forums and we need not review that success story in detail here. For example, a substantial record was recently developed in Ex Parte 658,[40] on the occasion of the 25th anniversary of the Staggers Act. The Department of Transportation's testimony in that docket perhaps most succinctly summarizes the record:

> The Department of Transportation considers the Act a resounding success. We do so because in sum the statute did what it was designed to do. It revitalized the railroad industry and by so doing benefitted shippers and consumers throughout the economy.[41]

The Board's Notice in this docket also appropriately acknowledges the role that deregulation played in advancing Congress's transportation policy goals: "These agency exemption decisions were instrumental in the U.S. rail system's transition from a heavily regulated, financially weak component of the economy into a mature, relatively healthy industry that operates with only minimal oversight."[42]

Second, by freeing the railroads from unnecessary regulation, the exemptions have benefitted both carriers and shippers in more concrete ways. As decisions by the ICC and later the Board concluded, the exemptions (1) reduced costs and enabled railroads to offer more efficient and responsive services; (2) allowed railroads to respond

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39 49 U.S.C. § 11101(1-2, 4-5).

40 *See generally The 25th Anniversary of the Staggers Rail Act of 1980: A Review and Look Ahead,* STB Ex Parte 658, NS Comments (Oct. 19, 2005); *Id.*, AAR Comments (Oct. 12, 2005).

41 *The 25th Anniversary of the Staggers Rail Act of 1980: A Review and Look Ahead,* STB Ex Parte No. 658, Transcript of Hearing (Oct. 19, 2005), pp. 14-15 (remarks of Paul Samuel Smith).

42 Corrected Notice, at 3.

more quickly to market forces; (3) enabled railroads to quote instantly-adjustable spot rates where appropriate; (4) reduced paperwork and other regulatory burdens; and (5) generally positioned railroads to compete more effectively against trucks and other modes.[43] Those findings were based on testimony by railroads and shippers alike, as well as on studies conducted by ICC staff in the late 1980s that examined the "impact of prior exemptions" and that "attest[ed] to numerous positive benefits to shippers and railroads."[44]

The Department of Transportation has twice ratified the benefits of exemptions. During Congress's consideration of ICCTA, DOT testified in favor of retaining the exemption authority and mandating its continued aggressive use by the Board, noting that "traffic exemptions have allowed railroads to retain or increase market share and meet competition by offering innovative rates and services without regulatory lag."[45] Ten years later, when the Board proposed a partial revocation of the commodity exemptions to permit regulation of fuel surcharges on exempt traffic, DOT reconfirmed these views.

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43 *See generally Rail General Exemption Authority – Miscellaneous Manufactured Commodities, Ex Parte No. 346 (Sub-No. 24)*, 6 I.C.C. 2d 186, 190-91 (1989) ("Our experience with other exemptions we have granted with regard to commodity groups and car types persuades us that this exemption will also result in substantial cost savings for the railroads, thereby increasing their efficiency, especially in the marketing of services."); *see also, e.g., Rail General Exemption Authority — Grease or Inedible Tallow*, ICC Ex Parte No. 346 (Sub-No. 31), 10 I.C.C.2d 453, 459 (1994) (noting that exemptions had enabled carriers to quote spot rates and eliminate costs associated with regulatory paperwork); *Rail General Exemption Authority — Ferrous Recyclables*, ICC Ex Parte No. 346 (Sub-No. 35), 10 I.C.C. 2d 635, 639–640 (1995) (same); *Rail General Exemption Authority — Hops*, Ex Parte No. 346 (Sub-No. 10), 365 I.C.C. 701, 702 (1982) (same).

44 *Miscellaneous Manufactured Commodities Exemption Decision*, 6 I.CC.2d at 191 n.8.

45 DOT ICCTA Testimony, at 217.

Reregulation would "unnecessarily and significantly cabin railroad discretion" and give unregulated truckers an unwarranted competitive advantage.[46]

In view of this record, it is not surprising that the Board has recently reiterated the conclusion that the exemptions have proven beneficial, and that unwinding them would have unpredictable and potentially harmful consequences:

> The exemptions permit the traffic involved (including intermodal traffic) to benefit from a competitive marketplace free of regulatory interference. Under the exemption, trucks and railroads compete on an equal footing for intermodal traffic, for example, with each competitor capable of adapting readily to changes in the marketplace. If we revoke the exemption, even partially, the railroads would be restricted in how they can respond to changes, while trucking companies would not. This kind of imbalance could have unintended consequences and upset the competitive balance between railroads and trucks.[47]

B. The Exemptions Continue to Be Important

Railroads continue to face far more extensive economic regulation than trucks and other transportation modes. The broad commodity exemptions granted by the Board and its predecessor therefore remain important even in today's less-regulated environment. To offer just a few examples:

- The commodity exemptions tend to level the competitive playing field with trucks and other modes. Unlike railroads, those modes do not face potential claims under ICCTA by shippers contending that their rates or practices are unreasonable. The need to guard against such claims and defend against them when they are brought – even when they lack merit – can impose significant costs and disruptions.[48] The commodity

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[46] DOT Comments in Ex Parte No. 661, at 6-7.

[47] *Rail Fuel Surcharges*, STB Ex Parte No. 661 (served Jan. 26, 2007), at 6.

[48] In the railroad rate-reasonableness setting, shipper claims are particularly costly because the Board generally does not render its market dominance determination until the end of a rate case, after the parties have spent substantial amounts of time and money to litigate the entire case.

(footnote continued on next page ...)

exemptions free the railroads from some of these burdens, while preserving the ability of shippers with truly meritorious claims to seek revocation and ultimately prevail.

- By freeing railroads, with respect to exempt services, from the common carrier obligation of Section 11101(a), the commodity exemptions give railroads the freedom to structure their service networks efficiently and make better use of scarce capacity by allowing them to decide when, whether and where to accept exempt traffic without an overhanging statutory obligation to do so.[49]

- By releasing railroads, with respect to exempt services, from the rate adjustment limitations of Section 11101(c), the commodity exemptions give railroads the same freedoms possessed by other transportation providers to adjust their rates (including surcharges, accessorial charges and the like) instantly in response to changing conditions.

- By exempting railroads, with respect to exempt services, from the car supply obligation of Section 11121(a), the exemptions allow railroads to focus their investments in areas of greater need and to manage more efficiently the equipment that otherwise would (if the exemptions were revoked) be needed to respond to potential demands for service.[50] For example, NS has made the decision not to invest in refrigerated cars for exempt perishables service.

There is no serious question that the exemptions have been and remain effective and important. The reduced regulation that results from the liberal granting of exemptions comports with Congress's mandate and furthers Congress's rail transportation policy objectives, by permitting railroads to compete with trucks, other

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See Gov't of the Territory of Guam v. Sea-Land Service. Inc., STB Docket No. WCC-101 (served Feb. 2, 2007), at 6.

[49] The Board has explained that the boxcar exemption does not exempt railroads from their common carrier obligations. *See Battaglia Distributing Co., Inc. v. Burlington Northern R.R.*, 2 S.T.B. 323, 329 n.13 (1997).

[50] The boxcar exception does not exempt railroads from their car supply obligations. 49 C.F.R. § 1039.14(a)(4)

modes, and one another, unburdened by the yoke of regulation that is no longer essential in the modern transportation environment.

III. THERE IS NO BASIS FOR RECONSIDERING THE EXEMPTIONS

Even if the Board had the power to revoke an exemption without a formal complaint, there is no conceivable basis upon which it could conclude that a wide-ranging revocation of the commodity exemptions – or any one of them – is warranted. There has not been any fundamental change in the competitive environment in which railroads operate that would establish any need for new regulation: railroads continue to face the same pervasive modal, intermodal, geographic and product competition that supported granting the exemptions.

A. The Exemptions Were Predicated on Findings of Pervasive Competition

Each of the exemptions was founded on extensive evidence establishing that regulation was not necessary to protect shippers from the abuse of market power.[51] As the Department of Transportation explained in 2006:

> [T]he fundamental premise for every exercise of this authority was that competition – intramodal, intermodal, product, and geographic – for the traffic in question was pervasive, rendering regulation

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[51] Certain of the commodity exemptions were granted on the basis that the service at issue was "of limited scope." *See, e.g., Rail General Exemption Authority— Liquid Iron Chloride*, Ex Parte No. 346 (Sub-No. 9A), 367 I.C.C. 347, 350–51 (1983) ("The comments show not only that relatively small quantities of liquid iron chloride are produced but also that the volume transported by rail is very limited. . . . Accordingly, we find, and the comments support, that transportation of liquid iron chloride is of limited scope."). The rail movement of these commodities is of equally "limited scope" today, and even if such traffic increased in importance, revocation would not be warranted absent a need to protect shippers from the abuse of market power. *See Rail General Exemption Authority—Fresh Fruits and Vegetables*, Ex Parte No. 346 (Sub-No. 1), 361 I.C.C. 211, 214 (1979) ("[T]he fact that in this case evidence of low market share has established the 'limited scope' requirement does not mean that the exemption would be revoked merely because rail participation in the exempted commodities might increase. Indeed, the 'limited scope' language does not appear in the statutory criteria for revoking exemptions.").

> unnecessary to carry out national rail transportation policy and protect against abuse of market power. That premise was validated separately for each commodity or equipment type, and only after a careful examination of all the relevant facts.[52]

Even a cursory review of the decisions granting these exemptions, and the court of appeals decisions consistently affirming them, reveals the various indicia of competition that justified the exemptions. In case after case, the agency and the courts relied on the presence of pervasive competition from other modes, especially trucks, as well as competition among railroads,[53] geographic and source competition,[54] or some

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[52] DOT Comments in Ex Parte No. 661, at 4-5.

[53] *See, e.g., Boxcar Exemption Decision*, 367 I.C.C. at 433 ("Shippers will not have to rely on truck competition alone to control boxcar rates. Alternate routes over different railroads are often available, especially over longer routes, giving shippers the benefit of intramodal price competition."); *Rail General Exemption Authority— Used Motor Vehicles*, Ex Parte No. 346 (Sub-No. 27A), 9 I.C.C. 2d 884, 886 ("There is also intense rail-to-rail and geographic competition because shippers have numerous options in selecting origin and destination points for used motor vehicle traffic and thus need not limit rail transportation to only one carrier.").

[54] *See, e.g., Rail General Exemption Authority – Exemption of Hydraulic Cement*, STB Ex Parte No. 346 (Sub-No. 34) (served Dec. 17, 1996), at 4 ("Dacotah's relatively unfavorable geographic location (usually the most distant supplier in the market it supplies) puts it at a natural disadvantage vis-a-vis its competitors. The carrier serving Dacotah must establish rates that overcome this disadvantage in order to handle Dacotah's hydraulic traffic. If the rate is too high, the producer does not participate in the market and the carrier does not participate in its transportation to that market."); *Rail General Exemption Authority— Ferrous Recyclables*, Ex Parte No. 346 (Sub-No. 35), 10 I.C.C. 2d 635, 641 (1995) ("Exceptionally strong geographic competition also exists, which further inhibits the railroads from dominating market power. Geographic competition occurs because these commodities, particularly iron and steel scrap, are produced and consumed throughout the United States."); *Rail General Exemption Authority— Carbon Dioxide*, Ex Parte No. 346 (Sub-No. 32), 10 I.C.C. 2d 359, 363 (1994) ("AAR and Carbonic have also submitted evidence of extensive geographic competition, which inhibits the railroads from exercising market power."); *Rail General Exemption Authority— Scrap Paper*, Ex Parte No. 346 (Sub-No. 12), 9 I.C.C. 2d 957, 960 (1993) ("Geographic competition occurs because scrap paper is generated throughout the Nation."); *Rail General Exemption Authority— Lumber or Wood Products*, Ex Parte No. 346 (Sub-No. 25), 7 I.C.C. 2d 673, 681 (1991) ("Geographic competition is particularly relevant for this lumber traffic because any attempt by a rail carrier to abuse market power by refusing to enter competitive joint rates or reciprocal switching agreements with other rail carriers would leave that carrier vulnerable to competition from other regions.").

combination of two or more of these. That competition was manifested in such factors as railroads' low share of traffic flows, railroads' relatively low margins, and the shipping characteristics of the commodities themselves, which at times reflected shippers' intrinsic transport options.[55] The agency's reliance on one or more of these factors was consistent with Congress's expectation that the Board would "examine all competitive transportation factors that restrain rail carriers' actions and that affect the market for transportation of the particular commodity or type of service" when considering whether particular traffic should be exempt from regulation.[56]

To be sure, the agency's decision to grant these exemptions did not reflect a conclusion that the abuse of market power was impossible in each and every conceivable set of circumstances within the scope of a commodity exemption. Withholding an exemption until "every shadow of a doubt" had been removed would have been inconsistent with the standard that Congress established.[57] Instead, the agency granted exemptions based on evidence of *generally-applicable* competitive conditions,

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[55] *See, e.g., Rail General Exemption Authority – Liquid Iron Chloride*, Ex Parte No. 346 (Sub-No. 9A), 367 I.C.C. 347, 349 (1983) ("The comments indicate that effective competition exists for the purchase and movement of liquid iron chloride, and that a substantial amount of that commodity moves via truck. The low and declining rail market share (27 percent in 1979; 10 percent in 1980), substantiates this claim."); *Rail General Exemption Authority – Hops*, Ex Parte No. 346 (Sub-No. 10), 365 I.C.C. 701, 702 (1982) ("In addition, abuses of market power are very unlikely to occur. As stated in our prior notice, the rail market share has been declining (from 38 percent in 1971 to 28 percent in 1980), and hops appear easily divertable to motor carriage, since they are moved in one-car lots (an average of 25.5 tons)."); *Rail General Exemption Authority – Scrap Paper*, Ex Parte No. 346 (Sub-No. 12), 9 I.C.C. 2d 957, 960 (1993) ("[T]he railroads' revenue-to-variable cost ratios for scrap paper range from 0.95 to 1.084. This indicates that many of the movements of this traffic produce relatively little, if any, net revenue and that the traffic thus is generally subject to significant competition. The presence of significant competition negates the potential for an abuse of market power.").

[56] *See* ICCTA Conference Report, at 169.

[57] *Boxcar Exemption Decision*, 367 I.C.C. at 440–41.

recognizing that it could deal with isolated pockets of market power using its revocation authority when those situations were brought to its attention by complaining shippers in need of protection.[58] This focus is reflected in the kinds of evidence of competition that figured most prominently in the decisions by the ICC and Board to grant the exemptions: *general* shipping characteristics; *widespread* availability of other modes of transportation providing both direct alternatives and indirect disciplining force (in the form of geographic and product competition); *aggregate* data on the percentage of shipments handled by railroad and other modes; and data on the *average* profitability of rail traffic.

There is no reason to believe that any of these general conditions has changed materially. To the contrary, the competitive forces relied upon by the ICC and Board to grant the exemptions remain as powerful today as they were 10, 20 or 30 years ago.

B. The Competition Relied on By the ICC and the Board in Granting the Exemptions Has Not Diminished

Given the continued prevalence of competition in the pertinent transportation markets, revoking the exemptions is not necessary to prevent the abuse of market power. In fact, absent a particularized showing of some "specific problem" that confronts a shipper or group of shippers with the threat of market power abuse, any revocation would be inconsistent with the evidence relied upon by the agency in granting the exemptions.

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[58] *See, e.g., id.* (recognizing that there could "exist[] a specific commodity that for some reason can be transported only by boxcar and on which the rate levels, being uncontrolled by intramodal competition or other market forces would rise to very high levels in the absence of regulation," but concluding that such "specific problems" should be dealt with "'after the fact,' not on a priori possibilities").

1. *Indirect Evidence of Pervasive Competition*

The decisions granting the commodity exemptions relied heavily on two types of evidence demonstrating that railroads faced pervasive competitive constraints for the commodities under review: (i) the railroads' typically small market share for such transportation and (ii) the railroads' relatively low profit margins, as reflected in average revenue-to-variable cost ratios.

These same metrics point in the same direction today. As a general matter, though railroads have worked hard to compete against trucks, they have not dramatically increased their market share of the exempt commodities, and – at least in NS's experience – rates for those commodities generally remain below the jurisdictional threshold. This evidence, NS submits, would support granting the exemptions all over again today. More importantly for present purposes, any movement towards a revocation of the exemptions could not be squared with the agency's reliance on such evidence in granting the exemptions.

At the most general level, railroads' share of the overall transportation marketplace has not grown in the last quarter-century. As DOT explained when it released its 2002 Commodity Flow Survey:

> Trucking continued its dominance of our nation's freight transportation system. In 2002, trucks hauled about 64 percent of the value, 58 percent of the tonnage, and 32 percent of the ton-miles of total shipments . . . , a slightly lower percentage of the value than in 1993, but more of the tons and ton-miles.[59]

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[59] Bureau of Transportation Statistics, U.S. Department of Transportation, Freight Shipments in America: Preliminary Highlights from the 2002 Commodity Flow Survey 10 (2004).

Since then, despite challenges posed by higher fuel costs, driver shortages, and additional safety restrictions, trucks handled 11 percent more tons in 2007 than in 2002, while the tonnage handled by railroads actually declined slightly over the same period.[60]

This broad trend is reflected in more recent data concerning movements of the exempt commodities. NS examined data for several of the commodity groups (at the 2-digit STCC level) for which a substantial portion of the individual commodities are exempt under Board regulations. Specifically, NS examined STCCs 14 (Nonmetallic Minerals); 24 (Lumber/Wood Products); 26 (Pulp/Paper); 29 (Petroleum/Coal Products); 32 (Clay/Concrete/Glass/Stone); 33 (Primary Metal Products); 37 (Transportation Equipment); 40 (Waste or Scrap).[61] For each of these commodity groups, railroads account for only a small minority of such shipments, as shown in Figure 1 below (and in the data set forth in Appendix Table 1).

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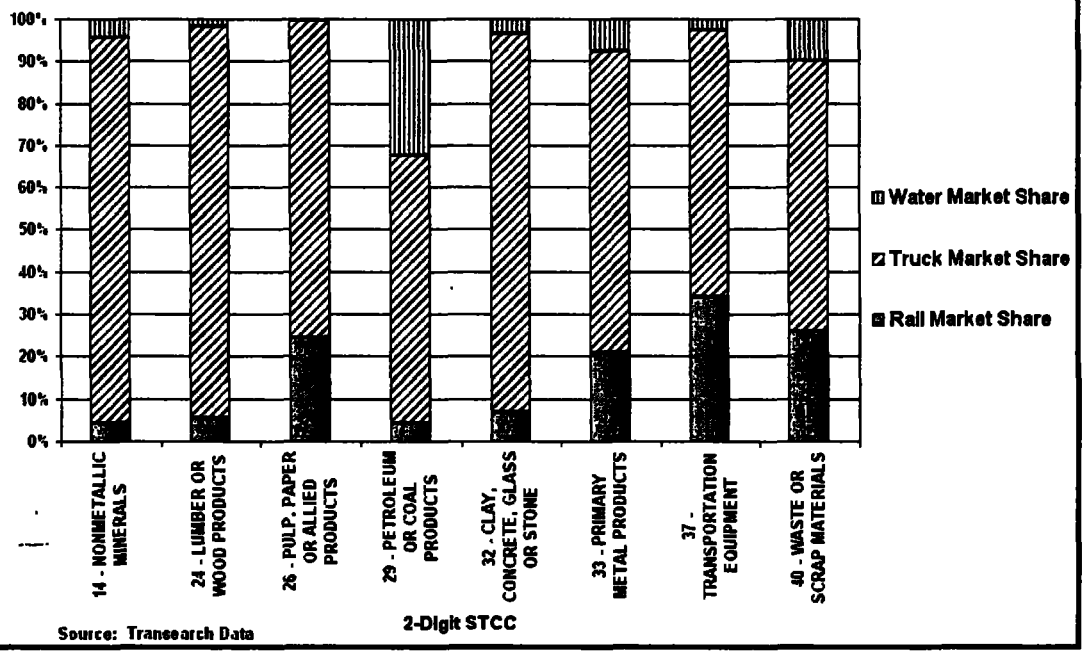
[60] *Compare* Bureau of Transportation Statistics, U.S. Department of Transportation 2002 Commodity Flow Survey Table 1a (2004) *with* Bureau of Transportation Statistics, U.S. Department of Transportation et. al., 2007 Commodity Flow Survey, Table 1c (2010).

[61] Approximately 80% of NS's exempt traffic is in one of these eight commodity groups.

Figure 1
2009 Modal Shares for Selected Commodity Groups



As the ICC and Board have long observed, relatively low railroad margins is another indicator of the presence of pervasive competitive constraints, precluding the exercise (much less abuse) of market power. Based on NS's experience handling exempt traffic, the vast majority of such traffic continues to move at rate levels well below 180 percent of variable cost.[62]

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[62] Of course, these metrics do not prove definitively that no railroad possesses market power with respect to any exempt traffic – any more than the same kinds of data established that fact when the exemptions were granted. Such an analysis could only be made based on particularized evidence in a revocation proceeding. It is telling, however, that shippers have not brought many such challenges, and nearly all of those they have brought have resulted in a conclusion that competition justifies applying the exemption to their circumstances. *Miscellaneous Manufactured Commodities Exemption Decision*, 6 I.CC.2d at 191 n.8 (commenting that as of late 1989 the ICC was aware of "fewer than a handful of petitions for revocation").

2. *Trucks Remain Omnipresent Competitors*

Another theme of many of the decisions granting the exemptions is the ready access of most shippers to efficient truck transportation.[63] In the years since the exemptions were granted, railroads have become more efficient and improved their service, but trucks have kept pace. Trucks today offer the same transportation options that they did when the exemptions were first established.

Motor carriers are physically able to serve each and every shipper facility that has rail access, whereas rail carriers are not able to serve directly many of the shipper locations reached by motor carriers. When shippers choose among alternative transportation providers, the characteristics that steer many of them to truck transportation are well known. Sometimes trucks may appear more expensive, but offer perceived service or other advantages that offset the rate differential and yield higher value.[64] On the other hand, sometimes rail may provide the best economic proposition. In all of these circumstances, however, attempts by railroads to raise rates or otherwise exploit shippers' preferences for rail movement would change the shippers' calculus and risk diversion of rail traffic to truck.[65] The vibrant competition that trucks offer thus is

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[63] *See, e.g., Boxcar Exemption Decision*, 367 I.C.C. at 433 ("The fundamental premise underlying the proposal for a boxcar exemption is that truck competition for the transportation of boxcar commodities is pervasive and limits the railroads' pricing freedom. . . .").

[64] *See, e.g.*, Brian A. Weatherford, et al., *The State of U.S. Railroads: A Review of Capacity and Performance Data*, RAND Supply Chain Policy Center 59 (2008) ("Despite the direct cost advantage of long-haul rail over long-haul truck, it is clear from the prevalence of national trucking firms that many companies find trucking to be more competitive or reliable."); *see also* AASHTO, *Freight-Rail Bottom Line Report*, pp. 13-14.

[65] As the Board explained in the *Boxcar Exemption Decision*: "Virtually anything that can be transported in a boxcar can be transported in a truck. Motor carriage tends to be faster, more accessible, more convenient, and sometimes less damaging to freight than rail service, *meaning that boxcar transportation generally must be priced to reflect these service differences to compete*

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not fully reflected in a static view of trucks' share of transportation flows, or even in a comparison of the relative cost of rail and truck transportation.[66]

Trucks offer especially attractive economics for shorter hauls, which in many cases account for the lion's share of all movements of exempt commodities. Trucks can compete effectively for various long-haul movements as well.[67] Even when trucks are not the preferred option for a given shipment, the widespread availability of truck transportation for other shippers of the same commodity disciplines rail transportation rates even for those shipments that would most naturally move by rail.

One railroad success story of the past several decades has been the growth in intermodal traffic, which has overtaken coal as the number one source of railroad revenue.[68] Needless to say, all exempt intermodal traffic moves via rail. However, railroads have tapped only a tiny fraction of the over-the-road transportation marketplace with their intermodal offerings. Over-the-road movement remains a viable (and often dominant) competitive option for both shorter and longer hauls:

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successfully. Thus, the market itself places an effective ceiling on rail rates for boxcar transportation, and regulation is unnecessary to assure that boxcar rates do not rise to unreasonably high levels." 367 I.C.C. at 433 (emphasis added).

66 As highlighted in the Comments in this proceeding of the Washington State Potato Commission (filed Jan. 14, 2011), potato shippers in Washington ship 93% of their potatoes by truck despite the fact that rail rates are supposedly lower than truck rates. They presumably make this choice because of other perceived advantages that trucks offer. In any event, these statistics confirm that rail has no market power that could be abused.

67 *See, e.g.*, National Cooperative Highway Research Program, No. 586, Rail Freight Solutions to Roadway Congestion – Final Report & Guidebook 7 (2007) ("There is no hard-and-fast distance that demarcates rail and trucking zones. Trucks provide some transcontinental service, while rail provides some local and regional services.").

68 *See id.* at G-40.

> For shorter hauls, all-truck movements tend to have cost advantages over intermodal movements, despite relatively high per-mile costs for trucks, as all-truck movements avoid "drayage" costs associated with hauling the container or trailer to and from railroad terminals, as well as the costs of loading and unloading the railroad flat cars. For longer hauls, truck shipments may have more desirable service qualities despite higher costs, although railroads have developed and expanded higher-speed and scheduled services in competition with trucking.[69]

In sum, the widespread and fierce truck competition that justified the exemptions originally remains a powerful constraint that prevents railroads from attaining or abusing market power.

3. *Railroad Competition*

For certain of the exempt commodities – including TOFC/COFC service, finished automobiles, and others – another critical factor in the grant of broad commodity-based exemptions was the existence of pervasive competition between railroads (both direct and via transloading). That competition is stronger than ever.[70]

Some critics of the Board's regulatory policies have suggested that modal competition has diminished as a result of the numerous major mergers approved by the Board and ICC in past decades. It is true that there are now fewer Class I carriers,[71] but it is not true that competition is less effective. Railroad consolidation in fact enhanced

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[69] Laurits R. Christensen Assoc., Inc., *A Study of Competition in the U.S. Freight R.R. Indus. and Analysis of Proposals that Might Enhance Competition*, Prepared for the Surface Transportation Board, 15-1 (Nov. 2009) ("Christensen Study").

[70] *See, e.g.*, Lawrence H. Kaufman, "Competition is alive and well," *Journal of Commerce*, May 21, 2007, at 27 ("Not only are railroads competing with trucks, they are competing vigorously with each other. Competition is alive and well.").

[71] Although there are fewer Class I railroads than when the Staggers Act was passed, "the total number of railroads has *increased* from about 490 in the mid-1980s to the current 559." Christensen Study, ES-8 (emphasis added).

competition by reducing railroad costs and enabling new and improved single-line and other services. These enhancements were among the many benefits underlying the Board's conclusions that the proposed transactions, as conditioned to preserve competition, were in the public interest. The benefits of these transactions have been validated by neutral retrospective analysis.[72]

And contrary to urban legend, these mergers did not extinguish rail shipping options. As the Department of Transportation explained to the Board in late 2005, "although there certainly ha[s] been a large, large number of mergers," in each merger case the agency imposed conditions that "sought to ensure that no rail shipper that was [served by] at least two carriers received less than that." As a result, DOT was "not aware of any merger related gain in the number of captive shippers."[73]

4. *Product and Geographic Competition*

As Congress intended, the STB and ICC have also granted several exemptions based on evidence that robust product and geographic competition would protect shippers from the exercise of railroad market power.[74] The Board's analyses took account of the

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[72] Even the most controversial of the mergers approved by the Board achieved meaningful benefits. *See* FTC Bureau of Economics, Working Paper No. 269, "*The Union Pacific/Southern Pacific Rail Merger: A Retrospective on Merger Benefits*," Denis A. Breen (Mar. 11, 2004) (published in Review of Network Economics) (concluding, *inter alia*, that "the rate reduction data submitted by UP during the course of the oversight proceedings, and the rate study conducted by STB staff were generally consistent with the UP/SP merger having a pro-competitive effect and meeting even a consumer welfare standard" and that "available evidence indicates that UP has documented the realization of substantial merger efficiencies of the types claimed"), *available at* http://www.ftc.gov/be/workpapers/wp269.pdf.

[73] *The 25th Anniversary of the Staggers Rail Act of 1980: A Review and Look Ahead*, STB Ex Parte No. 658, Transcript of Hearing (Oct. 19, 2005), pp. 22-23 (remarks of Paul Samuel Smith).

[74] *See* note 53, above.

fact that, although certain shippers served by only a single rail carrier may not have viable transportation alternatives for certain shipments, competing producers (or receivers) of the same or substitute commodities often do have transportation options that make it impossible for the sole-serving rail carrier to exercise any market power.[75] Product and geographic competition is no less robust today for many commodities, and – depending on the specific circumstances – would pose an obstacle to any shipper's assertion in a revocation proceeding that reregulation was needed to protect it from an abuse of market power.

C. No Other Developments Over the Past 30 Years Are Relevant to the Continued Vitality of the Exemptions

While there have been a variety of other changes in the railroad landscape over the three decades since enactment of the Staggers Act, none calls into question the soundness of the exemptions, much less undermines Congress's determination that those exemptions continue to play a vital role in the ongoing deregulation of the railroad industry.

1. *Trend Towards Reduced Regulatory Burdens*

One notable change, of course, has been the trend toward reduced regulatory burdens facing railroads, even for non-exempt commodities. The Staggers Act gave railroads a wide array of new rate-setting freedoms, and ICCTA continued that trend by, among other things, eliminating most tariff filing requirements.[76] To view this trend as

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[75] *See, e.g., Rail General Exemption Authority – Exemption of Hydraulic Cement*, STB Ex Parte No. 346 (Sub-No. 34) (served Dec. 17, 1996), at 4.

[76] ICCTA "eliminated the requirement that rail carriers file with the government tariffs containing the specific rates charges (or the basis for calculating them) for their common carriage

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calling into question the continued vitality of the commodity exemptions would turn Congress's deregulatory objectives upside down.

Congress affirmatively desired that the Board's exemption authority be used to *supplement* Congress's own ongoing deregulatory changes in the statutory framework. Congress viewed the Board's exemption authority as a "crucially important" means of "*expanding* existing statutory deregulation,"[77] not as an accordion that should be contracted as other regulatory burdens were relaxed. The fact that Congress directed the Board to exercise its exemption authority to the "maximum extent" while simultaneously removing some of the remaining day-to-day regulatory burdens facing the railroads – such as the tariff filing requirement – precludes the Board from altering course based on changes in the regulatory landscape. Congress did not want the Board to *re-regulate* while Congress continued to deregulate.

Moreover, the ICC long ago considered and rejected the argument that reductions in generally-applicable regulatory burdens diminish the importance of exempting traffic from regulation. Prior to the Staggers Act, the ICC could not grant an exemption without finding that "regulation was unduly burdensome and served no useful purpose."[78] The Staggers Act "eliminate[d] the test of burdensomeness" and instead *required* the ICC to grant exemptions "whenever continued regulation is unnecessary."[79] The same mandate

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transportation services." *See Disclosure, Publication, & Notice of Change of Rates & Other Service Terms for Rail Common Carriage,* Ex Parte No. 528, 1 S.T.B. 153, 153 (1996).

77 ICCTA House Report, at 96 (emphasis added).

78 *Boxcar Exemption Decision*, 367 I.C.C. at 428.

79 *Id.*

remains in place today. To revoke an exemption on the basis of generally reduced regulatory burdens would "fundamentally misconceive[]" Congress's mandate:

> Congress has directed that the Commission *shall* grant exemptions wherever it finds that continued regulation is *not necessary*. The ultimate issue is not whether regulation is harmless, but only whether it *must* be retained to carry out the rail transportation policy and protect shippers from market power abuse. If regulation is not necessary under these criteria, our instructions are to grant the exemption.[80]

Because the statutory scheme demands that revocation turn solely on the question whether regulation is necessary to prevent the abuse of market power, the fact that the railroads may face a lower regulatory burden than in the past does not – and can not – justify revocation.[81]

2. *Improvements in the Industry's Financial Health*

Some shippers have from time to time suggested that the increasing financial health of railroads warrants heightened regulation of railroad activities. This view is inconsistent with both Congress's rail transportation policy and the law in general. Progress towards revenue adequacy – and other indicia of the industry's improving health – was an affirmative *goal* of deregulation, not a basis for re-regulation. It bears remembering, moreover, that railroads had already made significant strides in improving their financial position by the time Congress decided to continue and re-invigorate its de-

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[80] *Id.* (emphasis in original).

[81] NS respectfully submits that the Board's consideration in *Rail General Exemption Authority— Exemption of Paints, Enamels, Lacquers, Shellacs, etc.*, Ex Parte No. 346 (Sub-No. 33) (served Apr. 20, 1998), at 6, of the relative benefit of the proposed exemption post-ICCTA cannot be reconciled with the statutory scheme. NS therefore understands the Board's decision to have rested instead principally on evidence "suggest[ing] that the railroads possess sufficient market power to justify continuing to provide shippers with recourse to challenge the rates charged for the transport of this traffic." *See id.* at 5.

regulatory thrust by enacting ICCTA. At every step in the evolution of today's legal and regulatory regime, that progress has been hailed as the crowning achievement of the regulatory reforms that began with the Staggers Act.[82] The exemptions were and remain a critical part of those reforms, and their success cannot support a return to regulation.

IV. THE BOARD SHOULD PROCEED TO EXAMINE THE APPROPRIATENESS OF EXEMPTING FROM REGULATION THE TRANSPORTATION OF ADDITIONAL COMMODITIES

NS submits that the Board's Notice (which indirectly questions "the relevance and/or necessity" of *existing* exemptions[83]) has it backwards. The Board should be asking if it has exempted *enough* of the railroads' traffic "'[T]he Commission [was] charged with the responsibility of *actively pursuing exemptions* for transportation and service that comply with the section's standards.'"[84] To carry out its statutory responsibilities, the Board thus should *actively* be pursuing the exemption of *additional commodities* for which regulation is no longer necessary to protect shippers from the abuse of market power.

NS has identified four commodities that account for meaningful rail volumes and as to which there appears to be no serious question that railroads lack market power.

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82 *See* discussion at pages 11-13, above.

83 Corrected Notice, at 3.

84 *American Trucking Assoc. v. ICC*, 656 F.2d 1115, 1119-20 (9th Cir. 1981) (quoting H.R. Rep. No. 96-1035, at 60 (1980), *reprinted in* 1980 U.S. Code Cong. & Ad. News 3978, 4005) (emphasis added).

At the seven-digit STCC level, those commodities are:

- Industrial Sand (1441310);
- Anhydrous Ethyl Alcohol (2818446);
- Phosphate Fertilizer Solution (2871450); and
- Asphalt (2911610).[85]

NS requests that the Board commence a proceeding pursuant to Section 10502(a) to review the appropriateness of granting additional exemptions covering these commodities.

In such a proceeding, NS would be prepared to provide evidence regarding the shipping characteristics of these commodities and the many competitive and other factors that preclude NS (and other railroads) from possessing, much less exercising, market power with respect to their transportation. For each of these commodities, railroads transport a small percentage of the total tons moved and face intense competition from trucks and other modes, as shown in Figure 2 below and Appendix Table 2. In addition, NS is confident that the Board would find that railroads earn low margins on the movement of these commodities, charging rates that on average yield revenue-variable cost ratios below the 180-percent jurisdictional floor.

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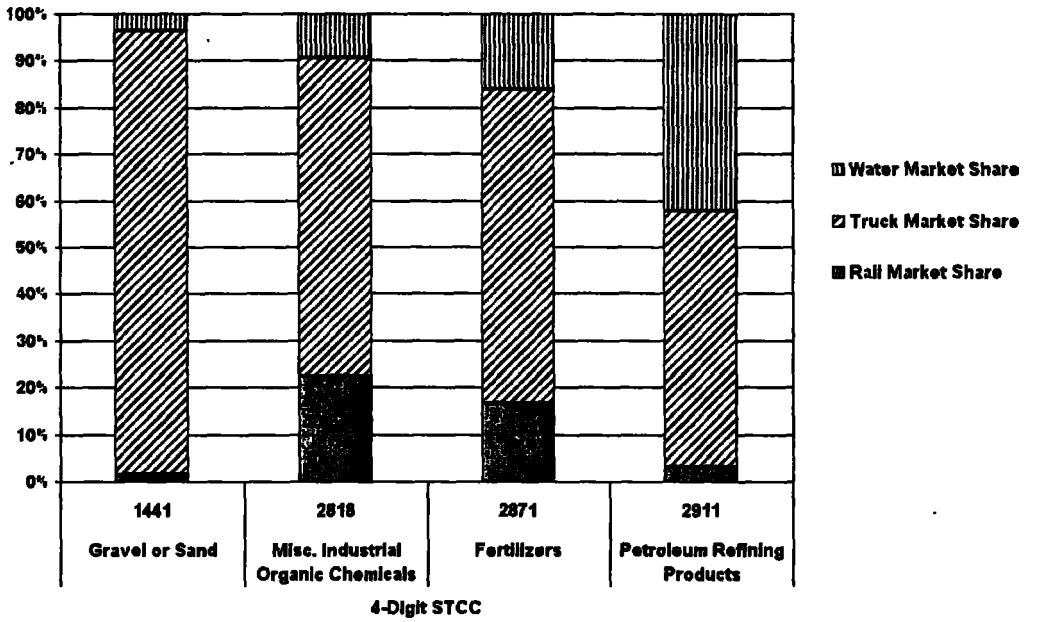
[85] NS believes that the Board has not previously considered exempting the transportation of Industrial Sand. The Board declined to exempt the other three commodities in *Misc. Manufactured Commodities*, Ex Parte No. 346 (Sub-No. 24), 6 I.C.C.2d 186 (1989), but that decision was not based on any finding that continued regulation was necessary to protect shippers from the abuse of market power. Instead, these commodities were not included within the scope of this exemption based on the inadequacy of the evidence submitted at that time to support their exemption.

Figure 2
2009 Modal Shares for Selected Commodity Groups



Source: Transearch Data

In these circumstances, NS submits that there is no realistic prospect that railroads could abuse any market power with respect to the transportation of any of these commodities, and they should therefore be exempted from regulation. The Board would necessarily retain its authority to remedy any future potential for market power abuse using its case-by-case revocation power. The Board accordingly should commence proceedings seeking comment on the proposed exemption of these additional commodities.

CONCLUSION

The Commodity, Boxcar and TOFC/COFC exemptions properly implement Congress's mandate to exempt rail traffic from regulation to the maximum extent consistent with the aim of protecting shippers from the abuse of market power. The Board should confirm the continued vitality of those exemptions, but remain open to

case-by-case consideration of particularized evidence demonstrating the need for the application of some Board-enforced regulation to protect particular shippers or groups of shippers from market power abuse.[86]

At the same time, in furtherance of Congress's mandate to exempt traffic from regulation to the maximum extent possible, the Board should commence proceedings to address the exemption of additional commodities as to which regulation is not needed to protect shippers from the abuse of market power.

Respectfully submitted,

James A. Hixon
John M. Scheib
Greg E. Summy
Christine I. Friedman
Norfolk Southern Railway Company
Three Commercial Place
Norfolk, VA 23510

David L. Meyer
Nicholas A. Datlowe
Morrison & Foerster LLP
2000 Pennsylvania Avenue, N.W.
Suite 6000
Washington, D.C. 20006

Attorneys for Norfolk Southern Railway Company

Dated: January 31, 2011

[86] In the course of any such review, of course, the Board would be bound to honor Congress's expectation that it will "examine all competitive transportation factors that restrain rail carriers' actions and that affect the market for transportation of the particular commodity or type of service for which revocation has been requested." ICCTA Conference Report at 169.

APPENDIX
TABLE 1
2009 MODAL SHARES*

STCC	Commodity	Total Tons	Tons by Rail	Tons by Truck	Tons by Water	Rail Share	Truck Share	Water Share
14	NONMETALLIC MINERALS	2,782,108,564	119,173,608	2,539,711,314	123,223,642	4%	91%	4%
24	LUMBER OR WOOD PRODUCTS	429,783,910	23,335,135	398,424,123	8,024,652	5%	93%	2%
26	PULP,PAPER OR ALLIED PRODUCTS	129,582,609	31,656,183	97,656,660	269,766	24%	75%	0%
29	PETROLEUM OR COAL PRODUCTS	915,805,888	39,096,763	580,762,834	295,946,291	4%	63%	32%
32	CLAY,CONCRETE,GLASS OR STONE	523,630,595	36,171,484	469,308,930	18,150,182	7%	90%	3%
33	PRIMARY METAL PRODUCTS	140,178,631	29,550,083	100,170,071	10,458,477	21%	71%	7%
37	TRANSPORTATION EQUIPMENT	88,239,120	30,200,776	55,733,837	2,304,506	34%	63%	3%
40	WASTE OR SCRAP MATERIALS	148,025,235	38,342,711	94,982,181	14,700,344	26%	64%	10%
TOTAL		**5,157,354,552**	**347,526,743**	**4,336,749,951**	**473,077,858**	**7%**	**84%**	**9%**

* - Source: TranSearch Data

APPENDIX
TABLE 2
2009 MODAL SHARES*

STCC	Commodity	Total Tons	Tons by Rail	Tons by Truck	Tons by Water	Rail Share	Truck Share	Water Share
1441	Gravel Or Sand	1,227,604,874	18,606,696	1,163,548,653	45,449,525	2%	95%	4%
2818	Misc Industrial Organic Chemicals	202,055,942	45,237,408	137,927,757	18,890,777	22%	68%	9%
2871	Fertilizers	85,576,371	14,302,802	57,417,250	13,856,319	17%	67%	16%
2911	Petroleum Refining Products	572,872,516	17,258,648	313,376,011	242,237,857	3%	55%	42%
TOTAL		**2,088,109,703**	**95,405,554**	**1,672,269,672**	**320,434,477**	**5%**	**80%**	**15%**

* - Source: TranSearch Data

SUMMARY OF TESTIMONY

OF

DAVID LAWSON

- My name is David Lawson, Vice President - Industrial Products for Norfolk Southern Railway Company. I have 23 years experience marketing rail service for both exempt and non-exempt commodities.
- Despite having met with hundreds of various customers, large and small and in a wide range of industries, in my 23 years, I have never once heard a single customer mention, much less complain about, the existence of any of the commodity exemptions or class of equipment/service exemptions (collectively, the "commodity exemptions" or "exempt commodities").
- I defer to the Comments submitted by Norfolk Southern's counsel regarding the legal standards applicable to commodity exemptions.
- What I can say based on my experience is that there certainly is no general *need* for regulation of any kind to prevent the abuse of market power by railroads with respect to the exempt commodities.
    - There are pervasive transportation options available to shippers for movement of the exempt commodities, including rail, trucks and other modes, as well as product and geographic competition.
    - These options discipline rail rates and service even in situations where a specific movement might be most effectively handled by rail.
    - I know from NS's experience that the rates for transportation of these commodities do not reflect the presence of any power that the railroads could abuse because rates are generally well below 180% of RCS variable costs.
- Any proceeding that the Board might commence to reevaluate of any of the exemptions on an across-the-board basis – not specifically focused on claims by a particular shipper or group of shippers concerning the potential, in their particular circumstances, for a serving railroad to abuse market power – would be both unwarranted and quite burdensome.
- Were the Board to go even further and *revoke* any of the exemptions in whole or in part, the effect would be even more disruptive and burdensome. To cite just a few examples:
    - As a general matter, NS's approach to exempt commodities – including rate setting, tariff rules, car supply and every other aspect of railroading – has for decades been dictated by the need to

compete (especially with trucks) rather than the need to comply with Board-administered regulation.

- Re-regulation of the exempt commodities would (again) un-level the playing field with trucks, which do not face the potential for burdensome and unmeritorious claims by shippers that particular rates or practices are "unreasonable," which are able to alter rates in response to market conditions, and which have no obligation to provide service when it does not fit their network efficiently. In the exempt commodity transportation markets, shippers can and will make decisions based upon competition in the marketplace.

- Re-imposition of the common carrier and car supply obligations for exempt traffic could interfere with railroads' need to make efficient capacity-expanding investments in their networks, for example by inhibiting the deployment of capital to areas of greatest need. Requiring capital expenditures in order to handle previously-exempt traffic that has ample other transportation alternatives is unnecessary and a waste of resources.

- Norfolk Southern respectfully suggests that the proper course for the Board to take as a result of these hearings would be to commence proceedings to exempt additional commodities from unnecessary regulation, as suggested in Norfolk Southern's Comments.

CERTIFICATE OF SERVICE

I, Nicholas A. Datlowe, certify that on this date a copy of the Comments of Norfolk Southern Railway Company and Summary of Testimony of David Lawson, filed on January 31, 2011, were served by email and by first-class mail, postage prepaid, on all parties of record.

Nicholas A. Datlowe

Dated: January 31, 2011